

Master Document –Audit Program

Activity Code 19420		Compliance Audit CAS 420
Version 5.0, dated April 2004		
B-1	Planning Considerations	
Purpose and Scope		
<p>1. The purpose of CAS compliance auditing is to determine if the contractor's policies, procedures, and practices used to estimate, accumulate, and report costs on Government contracts and subcontracts comply with the requirements of CAS. CAS 420 establishes criteria for the accumulation of IR&D/B&P costs and for the allocation of such costs to cost objectives. FAR 52.230-2, Cost Accounting Standards, requires the contractor to comply with the CAS 420 criteria (48 CFR 9904.420). FAR 31.205-18 makes CAS 420 partially applicable to all contracts, even contracts which are not CAS covered or subject only to modified CAS coverage.</p>		
<p>2. The scope of this audit should generally be limited to the contractor's current fiscal year (CCFY). Some limited testing of prior year's transactions, especially unaudited fiscal years, is acceptable to assure that no system changes were made and no noncompliances exist. For efficiency, CAS compliance testing, if possible, should be performed concurrently with tests for compliance with FAR and contract terms.</p>		
<p>3. This program is intended to provide for the proper planning, performance, and reporting on the contractor's compliance with CAS 420. The audit steps in the program should reflect a documented understanding between the auditor, the technical specialist and/or the supervisor as to the scope required to comply in an efficient and effective manner with generally accepted auditing standards and DCAA objectives. The program steps are intended as general guidance and should be tailored as determined by audit risk.</p>		
Other Planning Considerations		
<p>1. Before beginning any CAS compliance audit, the auditor should first determine the contractor is subject to the CAS coverage. If the standard is not applicable to the contractor or no noncompliance with the standard overall has no significant impact on Government contract costs, there is no need to test whether the contractor is complying with the standard. The decision to not test for CAS compliance should be documented (see CAM 8-305 and DoD CAS Working Group Guidance Paper 76-7).</p>		
<p>2. Materiality (see 48 CFR 9903.305) and audit risk assessment (including Internal Control Audit Planning Summary (ICAPS) for major contractors, ICQ for nonmajors, and historical CAS problems) are integral parts of the planning process and should be considered in developing the extent and frequency of CAS compliance tests.</p>		

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3. Once it is determined that the standard is applicable and material to the Government, the auditor should assess which provisions of the standard are significant to the contractor; the extent of reliance that may be placed on the contractor's system of internal controls to ensure compliance; and the results of other relevant audits (e.g., results of prior compliance audits, Disclosure Statement examinations, etc.). The decision to not test whether the contractor is complying with specific provisions of the standard should be documented.

B-1	Preliminary Steps	WP Reference
Version 5.0, dated April 2004		
1. Research and Planning		
a.	Read and become familiar with the criteria in CAS 420, CAM 7-1500, 8-420, and any recent Headquarters guidance not incorporated in CAM.	
b.	Evaluate applicable parts of the contractor's Disclosure Statement (e.g., Parts II, III, IV and VIII) to become familiar with the disclosed accounting practices. Determine if the contractor's accounting practices have remained unchanged since the last CAS compliance audit. If changes have occurred, adjust audit scope accordingly.	
c.	Evaluate recent forward pricing or incurred cost proposals to determine whether total costs subject to CAS 420 are material. Consider contractor's sales mix (i.e., CAS-covered Government contracts vs. non-CAS-covered and commercial). If not material, discuss with supervisory auditor before continuing audit.	
d.	Examine other FAO permanent file data (e.g. relevant audit leads, MAARs Control Log, etc.) and prior relevant audit work packages to determine what data are available, what audit steps were done in the past, and the results from those steps. This will identify areas of high risk and/or areas where limited or no compliance testing is necessary. Document results.	
e.	Discuss the planned compliance audit with the administrative contracting officer and, if appropriate, other customers to identify, understand, and document any concerns they may have or areas, which should be evaluated.	
2. Entrance Conference		

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a. Arrange and conduct an entrance conference covering the areas highlighted in CAM 4-302 with particular emphasis on:	
(1) Requesting the contractor's explanation of the internal control structure as related to CAS 420.	
(2) Any changes since the last audit.	
(3) The contractor's monitoring process for classifying costs.	
(4) Any identified weaknesses which may have been reported and related follow-up actions.	
b. If reliance is to be placed on the work of others, the file should contain the required documentation (see CAM 4-1000).	
3. Risk Assessment Steps	
a. Examine the ICQ or ICAPS, whichever is applicable, to obtain information regarding accounting system adequacy, identify any known outstanding system deficiencies, and perform preliminary assessment of risk.	
b. If the contractor is classified as non-major (where ICAPS have not been completed) and if the evidential matter to be obtained during the audit is highly dependent on computerized information systems, document on working paper B-2 the audit work performed that supports reliance on the computer-based evidential matter. Specifically, document or reference one or more of the following on working paper B-2:	
(1.)The audit assignment(s) where the reliability of the data was sufficiently established in other DCAA audits,	
(2.)The procedures/tests that will be performed in this audit to evaluate the incurred costs that will also support reliance on the evidential matter, and'	
(3.)The tests that will be performed in this audit that will be specifically designed to test the reliability of the computer-based data.	
When sufficient work is not performed to determine reliability (i.e., reduce audit risk to an acceptable level), qualify the audit report in accordance with CAM 10-210.4a and 10-807.3.	
c. Document assessment of the contractor's internal control structure relative to this standard (control environment, accounting system, and relevant policies, procedures, and practices) to assure	

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compliance with laws and regulations. Identify areas of potential high risk that would require increased transaction testing for compliance with CAS 420. The auditor should also document areas where limited or no transaction testing would be required based on the above control objectives assessment of risk.	
<p>d. In planning and performing the examination, review the fraud risk indicators in CAM Figure 4-7-3 for applicability to this audit. Document in working paper B any identified fraud risk indicators and your response/actions to those identified risks (either individually, or in combination). This should be done at the planning stage of the audit as well as during the audit if risk indicators are disclosed. If no risk indicators are identified, document this in working paper B.</p> <p>e. From the information gathered in the preceding steps and using the materiality criteria in 48 CFR 9903.305, assess the audit risk and determine the scope of audit and extent of compliance testing to be performed.</p>	
f. Update the information in the permanent files as needed.	

C-1	Accumulation of IR&D / B&P Costs by Project (MAAR 17)	WP Reference
Version 5.0, dated April 2004		
1.	Analyze job cost ledgers/reports to determine that the cost accumulation system identifies and segregates significant IR&D/B&P effort by individual project (CAS 420.40(a)). Costs of immaterial IR&D or B&P projects may be combined within each category.	
2.	Determine proper classification of IR&D/B&P effort by evaluating work authorizations, statement of work or any other similar documents. Ensure that the effort charged as IR&D or B&P is neither sponsored by a grant, nor required in performance of a contract. (CAS 420.30(a)(2) and (6)).	
3.	Evaluate detailed job cost report to determine that the costs for each IR&D/B&P project include all direct costs for IR&D/B&P projects (CAS 420.40(b) and 50(a)(1)). Direct costs are those costs, which if incurred in like circumstances for a final cost objective, would be treated as direct costs of that final cost objective.	
4.	Evaluate the most recent incurred cost submission or forward pricing rate proposal to determine all allocable overhead costs (except business unit general and administrative (G&A) expenses) of productive activities and other indirect costs (e.g., service center costs) related to the project applied to the direct costs, based on the	

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contractor's cost accounting practices (CAS 420.40(b) and 50(a)(2)).	
5. Evaluate the charging practices for IR&D effort and B&P administration costs to determine that such costs are consistently treated the same in like circumstances. They are to be treated as direct charges, which, if incurred for a final cost objective, would be charged direct to contracts. Otherwise, they should be treated as indirect expenses (CAS 420.50(a) and 60(a)).	
6. Evaluate the most recent incurred cost submission or forward pricing rate proposal to determine that the IR&D/B&P project costs exclude G&A expense (CAS 420.40(b)).	

D-1	Accumulation of IR&D / B&P Costs by Pool	WP Reference
Version 5.0, dated April 2004		
1.	Determine that IR&D/B&P costs are accumulated in a separate pool apart from the G&A pool (CAS 420.40(c)).	
2.	Determine that the IR&D/B&P pool costs consist of only:	
	a. IR&D/B&P project costs exclusive of G&A (see Step 1 above)	
	b. Allocable home office IR&D/B&P costs (see W/P E-1, Allocation to Cost Objectives, Step 3.)	
3.	Determine that the contractor has consistent and equitable practices regarding B&P costs resulting from a specific requirement of an existing contract. (CAS 402.61(c))	

E-1	Allocation to Cost Objectives	WP Reference
Version 5.0, dated April 2004		
1.	Evaluate the objectives and/or work statements for IR&D/B&P projects and identify those projects, which benefit only the performing segment and those benefiting other segments as well.	
2.	When the project(s) benefit other segments, determine whether the project costs need to be transferred to the home office. Such project costs need not be transferred to the home office when a direct allocation to the segments is not substantially different from the allocation which would be made if they were to pass through the home office (CAS 420.50(d) and (g)).	
3.	For those projects which have been identified as benefiting more than one segment in step 2 above, determine that the project(s) are	

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transferred to the home office exclusive of G&A. If the work is not a part of an IR&D/B&P project of the performing segment, then transferred costs should include G&A (CAS 420.50(d)).	
4. For those projects which only benefit the performing segment, determine that the project costs are included in the IR&D/B&P pool and allocated on the same base used by the segment to allocate G&A expense under CAS 410 (CAS 420.50(f)(2)). (MAAR 18)	

F-1	Inter-Segment IR&D / B&P Effort	WP Reference
Version 5.0, dated April 2004		
1.	Auditors located at segments performing IR&D/B&P effort for another segment must determine whether such effort is part of an IR&D/B&P project of the performing segment.	
a.	Coordinate this determination with the CAC, home office auditor, and/or the auditor at the receiving division prior to proceeding to the next step in the audit program.	
b.	When such effort is part of the performing segment's IR&D/B&P project, determine that the project costs are transferred to the home office exclusive of the segment's G&A.	

G-1	Deferral of IR&D / B&P Costs	WP Reference
Version 5.0, dated April 2004		
1.	Determine that all B&P costs incurred during a cost accounting period are assigned to that period only. (CAS 420.40(f)(1)).	
2.	Determine that all IR&D costs incurred during a cost accounting period are assigned to that period except as may be permitted by provisions of existing laws, regulations, and other controlling factors. (CAS 420.40(f)(2)).	

H-1	Home Office IR&D / B&P Costs	WP Reference
Version 5.0, dated April 2004		
1.	Coordination with segment auditors regarding accumulation of IR&D/B&P costs by the home office:	

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a. Coordination with the segment auditor(s) will be required to identify:	
(1) Those IR&D/B&P projects which will benefit some segments or all segments.	
(2) Inter-segment IR&D/B&P projects that are part of the IR&D/B&P project of the performing segment.	
b. For those projects which have been identified as benefiting more than one segment, determine that the costs of such projects have been transferred to the home office from these segments.	
c. Determine that the home office cost accumulation system for such costs is in sufficient detail so that the allocation to the segments can be made in accordance with the allocation requirements identified in Step 2. below.	
2. Allocation to Segments – Evaluate the allocation(s) of home office IR&D/B&P project costs to the segments to determine that:	
a. Direct allocations are first made for those projects that can be identified with specific segments (CAS 420.50(e)(1)). Determine if the method used to allocate the costs to more than one segment is based on the beneficial or causal relationships between the projects and the segment.	
b. Those other projects, remaining after the direct allocations are made to specific segments, are allocated among all segments by means of the same base used to allocate the residual expenses in accordance with CAS 403 (CAS 420.50(e)(2)).	

A-1	Concluding Steps	WP Reference
Version 5.0, dated April 2004		
1.	Summarize the results of audit.	
2.	Discuss results with the supervisor and/or the FAO technical specialist. The auditor should only report those noncompliances which are considered material (see CAM 8-302.7).	
3.	Coordinate significant or unusual issues with the CFAO, FAO Manager, and if applicable, with the CAC, CHOA, or GAC network (see CAM 8-302.4 8-302.6). Coordination should be both before and after discussion of results with the contractor. The CFAO should be apprised of noncompliance matters at the earliest possible date. If a noncompliance is considered immaterial, recommend to the CFAO that the contractor be notified to reserve the Government's right should	

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the cost impact become material (see FAR 30.602).	
4. Prepare draft audit report in accordance with CAM 10-807 (activity code 194XX) when no instances of noncompliances are found, or CAM 10-808 (activity code 19200) when instances of noncompliances are found.	
5. Conduct an exit conference with the contractor in accordance with CAM 4-304.	
6. Finalize audit report incorporating the contractor's response and audit rejoinder, if applicable.	
7. Closing actions should be performed in accordance with FAO procedures. These procedures may require either auditors or administrative personnel to perform various closing steps. Completion of these closing actions should be documented (e.g., by initials and date on the CD or working paper folder, etc.) and should include:	
a. The title, author, and keywords fields of the file properties in the audit report must be completed (for the audit report only) prior to final filing.	
b. Review the APPS exe file for size. APPS-generated executable files that are over 10 megabytes in size should be reviewed to ensure that the format and content justify the size. Supervisors are responsible for reviewing or designating someone to review these files for content and format.	
c. Review the APPS exe file for temporary files. These files can be recognized by the “~\$” or “~WRL” at the beginning of the file name. Once the APPS exe file is complete and there is NO ACTIVITY to be completed on any of the files contained within the exe file, any temporary files should be deleted so there are no unintentional versions of working papers and/or reports. NOTE: This should be done prior to invoking the Export/Archive Option in APPS.	
d. Once an audit report is signed, the electronic document should immediately be modified to indicate who signed it, and it should be password protected. The electronic file should then be renamed according to the convention “01 DCAA Report [RORG-ASSIGNMENT NO.] – Final.doc” and changed to a read-only file. Only this file should be stored, transmitted, or otherwise used for official purposes. For Memorandums the word “Report” would be replaced by “MFF” or “MFR” in the naming convention as appropriate.	
e. When the audit report is transmitted electronically to the requestor, the transmission email should be saved as a txt file (this will ensure the attachments are not saved again). Saving delivery or	

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read receipts is optional. If saved, the naming convention should distinguish them from transmittal emails.	
f. Once the report is signed, the signature page of the audit report must be scanned in accordance with Agency standard scanning instructions. For audit packages, the scanned signature page file should be named the same as the audit report (see above) with “-sig” added (i.e., 01 DCAA Report 01101-2002X10100389-Final-sig.pdf). There is no requirement to make the file a part of the APPS generated executable file and it must be included separately in the iRIMS folder. There is no need to scan the signature page of a Memorandum unless it is distributed outside of DCAA.	
g. Ensure an electronic copy of the final draft audit report containing the supervisory auditor’s initials and date, cross-referenced to the working papers, is included in the working paper package. The final draft report should include all substantive changes made to the original draft, with cross-referencing updated as necessary. It should differ from the final report only due to minor administrative changes (spelling, format, etc.) made during final processing.	
h. Ensure all working paper files are "read only" and, if necessary, compressed for final storage. Generally, current Agency software should be used to automatically modify all electronic files for storage.	
i. Two complete sets of electronic working papers should be filed. One set (official) will be filed in iRIMS. A second set (backup) will be stored on removable media in the hard copy working paper folder. The new APPS naming convention (ex: 01701_2003A10100001_Archive_093003.exe) will be used for both. If there will be a short-term need to access the working papers, a third, or "working" set should be stored so as to be available for reference, generally on the LAN. This set should be deleted when no longer needed.	
j. Verify using a separate machine, that electronic files stored on removable media are not corrupted and can be unarchived. Indicate the test was successful by placing tester initials and date prominently on the CD label.	
k. Securely enclose the “backup” set of electronic files (CD) and any “official” set of hard copy in the hard copy folder.	
l. File the “official” set of electronic files in iRIMS (see iRIMS User Guide).	
m. <u>Do Not File Sensitive Audits in iRIMS</u> : Sensitive audits include but are not limited to classified work, suspected irregular conduct, hotline or DCAA Form 2000 related files. These audits should not be filed in iRIMS at this time. See CAM 4-407f for filing	

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instructions.	
8. Update the permanent files, relevant ICAPS, or ICQ, and MAARS schedules. <i>Ensure that a copy of DMIS Report No. CAS 3 entitled “CAS Compliance Testing (Activity Code 194XX)” is included in the permanent file after the assignment has been closed in DMIS.</i>	